June 20, 2007

Mr. Winston Hickox
Chair, AB 32 Market Advisory Committee
California Environmental Protection Agency
Sacramento, CA 95814

Dear Mr. Hickox,

The AB 32 Implementation Group is a large and growing coalition of companies working towards the effective implementation of AB 32 and other California climate change policies. The overarching principles guiding the coalition can be found on our website at www.ab32ig.com.

We appreciate the hard work of the members of the Market Advisory Committee and their thoughtful report. We agree with the report's major findings that a cap and trade system will help us meet the twin goals of AB 32: to achieve ambitious emission reduction goals and to protect our growing California economy.

It's worth repeating that the goal of reducing greenhouse emissions to impact climate change is different from typical pollution reduction goals. To impact climate change, the total concentration of greenhouse gases in the atmosphere must be managed. There is no site specific negative health impact of CO2 emissions. And no matter where, when, or how emissions are created, the impact on climate is the same. This makes a cap & trade system particularly appropriate to achieve emission reductions at the least cost which is the goal of AB 32.

Of course, there are important choices to make in the design of the cap and trade program. The good news is that there is a wealth of experience with successful cap and trade programs: The Clean Air Act's program that cut sulfur dioxide emissions in half with a savings of $1 billion a year. Cap and trade also has been used to phase out leaded gasoline and ozone depleting substances such as chlorofluorocarbons. Europe's cap and trade system is expected to account for roughly 50% of the greenhouse gas emissions needed to meet its global warming reduction goals.

The AB 32 IG does not at this time have a fully developed and specific recommendation for the design of the cap and trade program. But based on our general principles, we support the recommendation to provide an offset, or credit, for emission reductions achieved by an entity in a sector that is not covered by a given cap and trade system. This broadens the reach of the program and helps achieve the overall emission reduction goals at a lower cost. We also support the recommendation to recognize and credit companies that take early actions to reduce emissions. Finally, we also support the recommendation for California to link with national and global carbon markets to lower costs even further.

However, we have some concerns with regard to how the report treats one of the key design choices to be made by policymakers – how to allocate emission allowances, the auction versus allocation debate.

We are concerned about using auctions for most or all of the allowances distribution. The auction of allowances is a decision to tax, up front, companies for the right to emit – an activity now allowed without restriction or cost. The report characterizes the alternative to auctions as a “free” allocation, which suggests a give-away or gift to companies, when in fact this activity is already freely available to companies.

Also, it’s important to acknowledge that an auction is like a tax, and that the design choice for policymakers is whether to impose a new tax on California companies and consumers in the form of an auction or not to impose an additional tax.

The dollar amount of the auction tax could reach billions. This would hurt not only California companies, but would likely be passed onto to consumers. In fact, on page 44, the report acknowledges electric consumers would pay a lesser price under allocations than under an auction system.

In addition, an auction tax unfairly penalizes companies that chose to invest, operate and create jobs in California. The auction tax would not be imposed on out-of-state or international competitors. California is already a high-cost state to operate businesses – this would add to our cost disadvantage and discourage new investments and expansions.

It is vital that we NOT discourage expansion and growth in California. Not only are jobs and government tax revenues at risk, an auction tax would also undermine our goals to achieve emission reductions. If we simply move emissions out of the state by discouraging in-state production, overall emissions would not decrease. In fact, since California and US companies are already the most energy efficient producers in the world, it is nearly certain that the production and imports from other countries will carry a higher greenhouse gas emission penalty than the in-state production that declined because of the tax. We would be *increasing* global emissions!

Finally, California is taking the lead in climate change policy. If we want other states and the federal government to follow our lead, it is important that we develop a program with broad public support. The public is generally reluctant to support new taxes and a cap & trade program that includes this component could hurt our overall efforts.

For all the reasons stated, we encourage policymakers to not adopt an auction tax for the cap and trade program.

Thank you.

Dorothy Rothrock
Vice-President
California Manufacturers &
Technology Association

Dominic DiMare
Vice-President
California Chamber of Commerce